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No. 02-1318

IN THE
Supreme Court of the United States

ZAPATA HERMANOS SUCESORES, S.A., PETITIONER,

v.

HEARTHSIDE BAKING CO. D/B/A MAURICE LENELL COOKY CO., RESPONDENT.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

SUPPLEMENTAL BRIEF FOR THE PETITIONER

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SUPPLEMENTAL BRIEF FOR THE PETITIONER

The Solicitor General's Amicus Brief reflects a disturbing lack of commitment to the obligations undertaken by the United States, through its ratification of the CISG, to foster a uniform body of international law governing the sale of goods. The Government openly advocates the Seventh Circuit's isolationist disregard of multiple foreign precedents interpreting CISG Article 74, and it disregards the canons of construction imposed by Article 7. Ironically, the arguments mustered by the Solicitor General actually provide compelling proof that the Seventh Circuit erred, that the questions presented are indeed unsettled and vitally important, and that these questions can only be answered with Supreme Court intervention.

I. The Solicitor General confirms the Seventh Circuit's erroneous reading of the CISG with his inability to offer any principled rationale for the Seventh Circuit's holding that is rooted in either the text or principles of the CISG. The Solicitor General argues (at 6) that attorneys' fees can never qualify as a recoverable "loss" under Article 74 because the recoverability of such fees is "an issue of procedure." Yet, he points to *nothing* in the text or history of the CISG supporting the conclusion that Article 74 draws any nebulous distinction between "substantive" and "procedural" losses. Indeed, "in interpreting international Conventions, all abstract distinctions between substantive and procedural laws become redundant, if not harmful, especially when the parties turn to the courts for equal enforcement of their contractual rights pursuant to these uniform bodies of rules." C. Orlandi, *Procedural Law Issues and Law Conventions*, V UNIFORM L. REV., 23, 24 (2000). The Government also never explains how the meaning or scope of Article 74 could plausibly be a "procedural" question left to the differing domestic laws of each signatory nation. Yet, as the Solicitor General concedes (at 8-9), that is the "inevitable" consequence of its position because Article 74's "substantive provisions [would then] be enforced through a variety of procedural means"—a result wholly at war with CISG's purpose of fostering "uniformity" in its interpretation.

The Solicitor General argues (at 6 n.1) that recovery of attorneys' fees is an "ancillary matter" not governed by contract law. That may be true when attorneys' fees are shifted automatically to a losing party under local procedure. But where, as here, attorneys' fees are sought as a component of the plaintiff's consequential *damages*, such recovery is necessarily governed by substantive contract law, in this case Article 74. As petitioner has explained (Pet. 17), the question presented here is *not* whether attorneys' fees should automatically be awarded to all prevailing plaintiffs under Article 74; it is whether such fees may be awarded as an element of a plaintiff's "loss" where Article 74's foreseeability requirements are met—just like any other form of recovcrable loss. Because this question turns on the text of the CISG itself, there can only be one answer to this question, and it is the obligation of every CISG signatory to find that answer in the text and principles of the CISG itself (see Art. 7), not in the varying mandates of domestic law.

In any event, the Solicitor General's view that the limits of Article 74 depend on the porous line between substance and procedure itself confirms the need for Supreme Court review because, as the Government acknowledges (at 6 n.1), "there may be some debate about whether attorneys' fees are properly construed as procedural or substantive." See also Pet. 17 n.7

The Solicitor General also argues (at 5) that attorneys' fees should not be recoverable as damages because Article 74 does not contain "any reference to attorneys' fees." But this too is plainly wrong, for if Article 74 is read only to permit the recovery of losses expressly mentioned, the provision would be meaningless since Article 74 "does not expressly mention *any* category of loss." Felemegas, 15 PACE L. REV. As the Second Circuit correctly held in *Delchi,* 71 F.3d at 1030, Article 74 is instead written in broadly *inclusive* terms to permit the recovery of *all* losses, "subject only to the familiar limitation that the breaching party must have foreseen, or should have foreseen, the loss as a probable consequence." And there is no indication anywhere in the CISG that signatories intended to *exclude*

attorneys' fees or any other category of loss from its scope. In cases like this where foreseeability is proven, the Solicitor General is simply wrong to argue (at 8) that there is "no reason to believe that any party to the Convention expected that a plaintiff's 'loss' would include its attorneys' fees." In such cases, the text of Article 74 *itself* confirms that expectation.

The Solicitor General also incorrectly assumes that any issue not expressly settled by the CISG must be resolved by domestic law. To the contrary, Article 7(2) requires that any "[q]uestions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which [the CISG] is based." The Government inexplicably ignores these principles *altogether*. For instance, it is undisputed that "one of the most fundamental general principles upon which the Convention based" is the principle of "full compensation"—a principle the district court prominently relied upon and held could only be satisfied "by freeing [a plaintiff's] damages recovery from the burden of attorneys' fees." Pet. App. 17a. The Solicitor General notably ignores this holding—as did the Seventh Circuit.

Even more disturbing, though, is the Government's striking lack of concern for the obligations undertaken by the United States "to promote uniformity in [the CISG's] application," and to foster the CISG's "expressly stated goal of developing uniform international contract law to promote international trade." *Asante Tech.*, 164 F.Supp. at 1151. Indeed, the Solicitor General's position reflects just the sort of "'island' or 'lone ranger' mentality" (to borrow Justice Ginsburg's recent phrase[1]) that the CISG was meant to eradicate. The Solicitor General openly defends the Seventh Circuit's disregard of foreign decisions construing Article 74 because "those decisions were rendered by courts and arbitration panels in only

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[1] Hon. Ruth Bader Ginsburg, Address to the Convention of the American Constitution Society, August 2, 2003. See www.americanconstitution-society.org/pdf/Ginsburgtranscriptfinal.pdf.

three countries (Germany, Switzerland, and France)"and because "none was rendered by the country's highest court"[2]—as if the views of appellate courts and other tribunals in these important signatory nations simply don't count. In the Solicitor General's view, it was also entirely proper for the Seventh Circuit to ignore these decisions in its opinion because "there is no reason to believe that it did not consider them." *Id.* at 11. But that is plainly wrong. To "promote uniformity in [the CISG's] application," courts *must* be required, at a minimum, to discuss precedents from other nations addressing similar issues. As Justice O'Connor has explained, while foreign decisions "are rarely binding upon our decisions in U.S. courts, conclusions reached by other countries and by the international community should at times constitute persuasive authority in American courts." 96 AM. SOC'Y INT'L L. PROC. 348, 350 (2002).That is particularly so here given the purpose of the CISG, and since "there is much to learn from other distinguished jurists who have given thought to the same difficult issues that we face here." *Ibid.*

While U.S. courts may not be *bound* by foreign decisions, U.S. courts must at least be required to explain why they are rejecting foreign precedents when they choose to do so. Without such dialogue, it will be impossible to foster the sort of "uniform interpretation" of the CISG that Article 7 requires. As Justice O'Connor recently noted in an address to the Southern Center for International Studies, "when it comes to the impression created by the treatment of foreign and international law and the United States courts, the jury is still out." *Atl. J. Const.* p. A3 (Oct. 29, 2003). Indeed, the Government's

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[2] The Government's assertion that none of the foreign decisions relied on in the Petition were decided by a country's highest court is wrong. As explained at Pet. 15, the Seventh Circuit's decision conflicts with the Austrian Supreme Court's holding that "[u]nder the second sentence of Art. 74, a claim for damages is *only* limited by the foreseeability of the loss for the party in breach." Case No. 1 Ob 292/99v (Apr. 28, 2000) (emphasis added).

position gives little comfort in this regard. Yet, the time for such myopic disregard of foreign precedent has long since passed. As Justice Breyer recently put it, "[b]y now * * * it should be clear that the chicken has broken out of the egg."[3]

The Solicitor General also argues that foreign decisions addressing the recoverability of attorneys' fees under Article 74 are entitled to no weight because they come from "loser-pays jurisdictions" where "attorneys' fees are available under domestic procedural law." Quite the contrary, the fact that other nations have held attorneys' fees to be recoverable under Article 74 even though certain fees could be shifted to losing parties under domestic law anyway confirms that their recoverability under Article 74 has nothing to do with domestic law. For instance, the German Court of Appeals in Düsseldorf (discussed at Pet. 10) awarded a plaintiff *certain* of its attorneys' fees pursuant to domestic procedural law, but ruled that the *remaining* attorneys' fees, which were *not* awardable domestically, were recoverable under Article 74 as *damages* in order to make the plaintiff whole. As such decisions confirm, allowing attorneys' fees to be recoverable under Article 74 would not, as the Solicitor General suggests (at 6), "displace the more general loser-pays rules *** that apply in other countries."

In sum, the Solicitor General's arguments on the merits in no way diminish the compelling grounds that warrant Supreme Court review. To the contrary, they actually *highlight* the unanswered questions that require this Court's definitive answer. Are losses recoverable under the CISG only if expressly mentioned in Article 74? Is the recoverability of attorneys' fees as a "loss" under Article 74 a procedural question governed by domestic law? Under what circumstances is a question "not settled" by the CISG? If a question is "not

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[3] Hon. Stephen G. Breyer, Keynote Address Before the 97th Annual Meeting of the American Society of International Law, April 4, 2003. See www.supremecourtus.gov/publicinfo/speeches/sp_04-04-03.html.

settled" by the CISG, may a court then resort to domestic law to answer it consistent with CISG Article 7(2)? What obligations do U.S. courts have to consider and discuss foreign precedents construing the CISG in order to foster a uniform interpretation of the CISG? This case provides an ideal opportunity for the Court to settle these questions once and for all, to resolve the international split of authority created by the Seventh Circuit, to address the CISG for the first time, and bring needed clarity and uniformity to this vitally important area of international commercial law.

II. The Solicitor General strangely accuses petitioner of overstating the circuit splits over the inherent power of federal courts to sanction bad faith conduct, when the Solicitor General's own Brief confirms that those conflicts do exist. In fact, the Government's Brief demonstrates that this case provides a unique opportunity for the Court to resolve *both* the question of whether the inherent power to sanction is limited by rules-based sanctioning mechanisms, and whether courts can consider pre-litigation conduct in deciding whether to sanction related bad faith conduct during the litigation process.

A. The Solicitor General's defense of the Seventh Circuit's inherent power holding hinges on his argument (at 15) that *Chambers* permits a court to exercise its inherent power to sanction only when rules-based sanctioning mechanisms are not "up to the task." But that argument begs the *very question* to be decided, and over which the circuits are deeply divided.

The Solicitor General claims (at 16) that there is no circuit split over whether the inherent power to sanction bad faith conduct extends only to conduct not covered by sanctions statutes or rules because petitioner "cites no decision" inconsistent with the rule that a court may only exercise its inherent authority to sanction when statutes or rules "are not up to the task." But this is demonstrably wrong. As the Government's Brief confirms (at 16-18), there are *nine* circuits rejecting the rule that the inherent power to sanction bad faith conduct extends only to conduct not sanctionable by rule, and

which thus *routinely* affirm inherent power sanctions without requiring *any* consideration of whether rules-based mechanisms are "up to the task." See Pet. 25-26; Reply Br. 7-9.[4] These circuits have relied on *Chambers'* statement that a court is not "forbidden to sanction bad-faith conduct by means of the inherent power simply because that conduct could also be sanctioned under the statute or the Rules." The Seventh Circuit, on the other hand, like the First and Third Circuits before it, reached exactly the opposite conclusion, holding that the courts' inherent power to sanction extends only to conduct "not adequately dealt with by other rules," and that the "limitations" of those rules "are equally limitations on inherent authority, which may not be used to amend the rules." Pet. App. 8a, 9a. The prejudice to petitioner from this circuit split is obvious, since the district court's sanction below would not have been

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[4] See, *e.g.*, *DLC Mgt. Corp.*, 163 F.3d at 136 (2d Cir.) ("the fact that there may be a statute or rule which provides a mechanism for imposing sanctions of a particular variety for a specific type of abuse does not limit a court's inherent power to fashion sanctions, even in situations similar or identical to those contemplated by the statute or rule"); *Travelers Ins. Co.*, 38 F.3d at 1418 (5th Cir.) ("a court is not forbidden from sanctioning bad-faith conduct under its inherent powers simply because that conduct could also be sanctioned under § 1927 or the Federal Rules of Civil Procedure"); *First Bank of Marietta*, 307 F.3d at 514 ("In our view, *Chambers* should be read broadly to permit the district court to resort to its inherent authority to sanction bad-faith conduct, even if the court has not expressly considered whether such conduct could be sanctioned under all potentially applicable rules or statutes"); *Fink*, 239 F.3d at 994 (9th Cir.) ("It is well settled * * * that the district court may, in its informed discretion, rely on inherent power rather than the federal rules or § 1927"); *Thomas*, 293 F.3d at 1328 n.32 (11th Cir.) ("That sanctions may have been possible under [statutes or rules] did not negate the district court's inherent power to levy sanctions against Munson for her misconduct"); *In re Mroz*, 65 F.3d at 1575 (11th Cir.) ("the 'inherent power of a court can be invoked even if procedural rules exist which sanction the same conduct,' for these rules are not substitutes for the inherent power"); *Pickholtz*, 284 F.3d at 1377 (Fed. Cir.) ("*Chambers* * * * permits, indeed requires, the court to separately consider [a] motion for attorney fees under its inherent power, which is an independent basis for assessing sanctions, one not preempted by Rule 37").

reversed in any of nine circuits for failure to determine whether Lenell's conduct could be sanctioned by statute or rule.

The Solicitor General tries to distinguish the majority cases on the ground that they contain "no finding that the conduct in question was in fact" sanctionable. U.S. Br. 17. But that is no distinction at all, and in fact misses *the whole point*. The fact that nine circuits uphold the imposition of inherent power sanctions without requiring any consideration of whether rules-based sanctioning mechanisms are "up to task," while three other circuits do impose that requirement, is itself the very circuit split that requires resolution by this Court. Indeed, the question squarely presented by this case is whether a court must find conduct not to be adequately dealt with by rules-based sanctions before it exercises its inherent power to sanction. It is simply undeniable that the circuits are deeply divided over this recurring and important question, which can only be resolved by this Court.

B. The Solicitor General also argues that there is no circuit split over whether a court may sanction purely pre-litigation conduct. We agree, but that is *not* the question presented. As the Solicitor General later acknowledges (at 15), the question also presented is whether a court may rely on pre-litigation conduct to sanction related bad faith conduct *during* the litigation. As to *this* important question, the Solicitor General makes no attempt to deny that the Seventh Circuit's decision irreconcilably conflicts with those of the Second, Fifth, Sixth and Eighth circuits. See Pet. 27-28. Instead, he merely observes (at 15) that "it is not clear that that question will have any significance in this case, because it is not clear how much of the conduct that gave rise to the fee award is properly classified as pre-litigation conduct." As the Seventh Circuit's decision makes plain, however, that classification makes no difference here at all.

The district court found that Lenell engaged in "extreme bad faith" through its pre-litigation refusal to pay an indisputable debt – bad faith conduct that then extended *into* the

litigation process when Lenell misused the judicial process to "make it as difficult and expensive as possible for Zapata to receive its money in this litigation" by "dramatically and needlessly expanding the scope of this litigation [and] interposing a host of unwarranted roadblocks" through "late-advanced, convoluted, multifarious and (regrettably) baseless defenses and counterclaims." Pet. App. 20a-22a, 23a, 25a.

Notwithstanding these specific findings of bad faith conduct during the litigation process, the Seventh Circuit vacated the district court's *entire* sanction simply because Lenell's bad faith conduct during the litigation was related to its *pre-litigation* refusal to pay. Pet. App. 7a. In the Seventh Circuit's view, conduct "giving rise to the litigation" is categorically off-limits, *regardless* of whether it relates to bad faith conduct during the litigation and how much of the fee award is attributed to the pre-litigation conduct, because otherwise "the punishment would be a product of substantive law." Pet. App. 7a.

As the Solicitor General's Brief acknowledges (at 14), the Seventh Circuit's holding irreconcilably conflicts with the Eighth Circuit's decision in *Lamb Eng'g,* which "adopted the view promulgated by various circuits that, in determining whether to award attorney fees based on the litigant's bad faith, '[t]he court may consider conduct both during and prior to the litigation, although the award may not be based solely on the conduct that led to the substantive claim.'" 103 F.3d at 1435. Accord *Sussman,* 56 F.3d at 459 (2nd Cir.) ("the court's inherent power is broader and would permit the court to impose sanctions on the basis of related bad-faith conduct prior to the commencement of the litigation"); *Shimman,* 744 F.2d at 1230, 1234 (6th Cir.) (inherent power to sanction extends to bad faith pre-litigation conduct "necessitating that an action be filed," particularly "where the defendant contumaciously refused to allow the plaintiff what was plainly owed, thus forcing the plaintiff to go to court"); *Perales,* 950 F.2d at 1071 (5th Cir.); *Ass'n of Flight Attendants,* 976 F.2d at 548-50 (9th Cir.).

It is difficult to imagine a case that more squarely presents the question of whether a court may rely on pre-litigation conduct in deciding to sanction related bad faith conduct during the litigation, both because the district court specifically found related acts of bad faith before and during the litigation, and because the Seventh Circuit foreclosed *any* consideration of pre-litigation conduct. In sum, the Solicitor General's Brief leaves no doubt that this case provides a unique opportunity for the Court to resolve *two* independently significant and recurring circuit splits over the limits of the federal courts' inherent power to sanction bad faith litigation conduct.

III. The Solicitor General lastly recommends that the Court deny the Petition because the Seventh Circuit's decision is somehow "interlocutory." That again is demonstrably wrong. The court of appeals fully and finally resolved petitioner's ability to seek attorneys' fees as damages under Article 74 of the CISG, and as a sanction pursuant to the courts' inherent power. The Solicitor General theorizes (at 18), however, that on remand the district court still could sanction Lenell for bad faith conduct if it finds that "*at least some* of that conduct is 'not adequately dealt with by other rules." (Emphasis added). But this affords no basis for denying the Petition for at least two reasons. First, the Seventh Circuit's holding that the Court's inherent power to sanction is subject to the procedural limits of Fed. R. Civ. P. 11 arguably precludes any further sanction since Rule 11 prohibits any sanction absent compliance with its notice and safe harbor provisions—compliance that is now impossible. And second, even if sanctions were still theoretically possible, petitioner would only be able to recover a fraction of the fees that were previously awarded. In short, affirmance or reversal by this Court would definitely resolve both questions presented and bring this litigation to an end.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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